

ORIGINAL

In the Matter of

CC Docket No. 01-324

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FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20054

In the Matter of)
)
Application by Verizon New England Inc.,)
Bell Atlantic Communications, Inc.)
(d/b/a Verizon Long Distance), NYNEX)
Long Distance Company (d/b/a Verizon)
Enterprise Solutions), Verizon Global)
Networks Inc., and Verizon Select Services)
Inc., for Authorization To Provide)
In-Region, InterLATA Services)
in Rhode Island)

CC Docket No. 01-324

COMMENTS OF SPRINT COMMUNICATIONS COMPANY L.P.

Sprint Communications Company L.P. opposes the above-captioned application of Verizon for authorization to provide in-region, interLATA services in Rhode Island.¹ The public interest requires that the application be denied unless the Commission is convinced that the local markets have been opened fully and irreversibly to competitive entry. In Sprint's view, this is not yet the case.

I. INTRODUCTION AND SUMMARY.

A key purpose of the 1996 amendments to the Communications Act of 1934 (the Act) was to open the local market to competition. To that end, Congress envisioned three avenues of local entry: resale, use of incumbent LEC unbundled network elements and

¹ Application by Verizon New England Inc., Bell Atlantic Communications, Inc. (d/b/a Verizon Long Distance), NYNEX Long Distance Company (d/b/a Verizon Enterprise Solutions), Verizon Global Networks Inc., and Verizon Select Services Inc., for Authorization to Provide In-Region, InterLATA Services in Rhode Island, CC Docket No. 01-324 (filed November 26, 2001) (Application).

facilities-based competition; and it placed incumbent LECs in the rather unnatural role of assisting their would-be competitors by imposing the interconnection, resale, unbundling and collocation obligations of § 251(c).

To encourage the principal ILECs – the BOCs – to cooperate in this process, Congress enacted the “carrot” of § 271, giving the BOCs the right to enter the long distance market in-region once their local markets were truly open. The Commission recognized the importance of local market competition in one of the first applications it decided under this section.

Although Congress replaced the MFJ’s structural approach, Congress nonetheless acknowledged the principles underlying that approach that BOC entry into the long distance market would be anticompetitive unless the BOCs’ market power in the local market was first demonstrably eroded by eliminating barriers to local competition. *** In order to effectuate Congress’ intent, we must make certain that the BOCs have taken real, significant and irreversible steps to open their markets. We further note that Congress plainly realized that, in the absence of significant Commission rulemaking and enforcement, and incentives all directed at compelling incumbent LECs to share their economies of scale and scope with their rivals, it would be highly unlikely that competition would develop in local exchange and exchange access markets to any discernable degree.²

If the BOCs are allowed to enjoy the § 271 “carrot” before local competition is fully established, they will have little incentive to cooperate with competitive LECs thereafter, unless they are subject to continuing regulation. Successfully maintaining such a regulatory structure and adapting it to changes in technology will require significant ongoing resources of both the Commission and interested parties, with, at best, uncertain

² Application of Ameritech Michigan Pursuant to Section 271 of the Communications Act of 1934, as amended, To Provide In-Region, InterLATA Services In Michigan, 12 FCC Rcd 20543, ¶18 (1997) (Michigan Order).

results. It would be far preferable to withhold the § 271 “carrot” until local competition is sufficiently entrenched that competitive forces can supplant the intensive regulation and enforcement that otherwise would be required. Sprint does not believe that point has yet been reached in Rhode Island. As shown below, the CLEC industry is in a state of crisis, and the RBOCs have failed to establish themselves outside their territory. In Rhode Island, a duopoly is emerging in the residential market, and competitors in the business market may be unviably small.

II. THE CLEC INDUSTRY IS IN A STATE OF CRISIS. (PUBLIC INTEREST)

The past year has been marked by the bankruptcy of many of the CLECs that were in the vanguard of the industry: Covad, e-Spire, NorthPoint, Rhythms, Teligent, WinStar and Convergent, to name a few.³ Most recently, on November 16, 2001, Net2000 filed voluntary petitions for relief under Chapter 11 and agreed to sell substantially all of its assets to Cavalier Telephone.⁴ It comes as no surprise that a Morgan Stanley analyst recently released a “dismal report” about the state of the CLEC industry, identifying several specific local carriers as likely candidates for formal restructuring.⁵

³ For a more complete list of CLECs that have filed for bankruptcy, *see* Comments of Sprint Communications Company L.P., In the matter of Joint Application by BellSouth Corporation, Inc., BellSouth Telecommunications, Inc., and BellSouth Long Distance, Inc. for Provision of In-Region InterLATA Services in Georgia and Louisiana, CC Docket No. 01-277, filed October 19, 2001, p. 6.

⁴ NET2000 Communications Inc (NTKK) Form 8-K, <http://biz.yahoo.com/e/011121/ntkk.html>.

⁵ Morgan Stanley: XO “Likely” to Restructure, Washtech.com, Brendan Barrett (October 9, 2001).

Faced with the expense and difficulty of building out local networks and with mounting losses, other CLECs have been forced to downsize. On October 3, 2001, McLeodUSA announced plans to reduce its workforce by 15 percent, consolidate 11 facilities into 3, sell non-core assets and excess inventory to generate between \$400 and \$450 million, and take a one-time non-cash charge of approximately \$2.9 billion.⁶ In its December 3, 2001 announcement of its recapitalization and financial restructuring plan, McLeodUSA stated that “it may pursue the administrative convenience of the court system through a voluntary pre-packaged Chapter 11 in order to achieve retirement of all outstanding bond issues and to accomplish the recapitalization in an expeditious manner.”⁷ Following McLeodUSA’s announcement, Reuters reported that McLeodUSA’s shares fell over 21 percent and “Moody’s Investor Service downgraded its distressed debt to one notch above its lowest grade.”⁸

XO Communications, another major local competitor, recently laid off 600 employees, approximately 8 percent of its workforce.⁹ On November 29, 2001, XO

⁶ McLeodUSA Press Room, “McLeodUSA Announces Focused Strategy for Future Growth, Abandons National Network, Identifies Non-Strategic Assets for Sale, Maintains Fully Funded Plan.”
<http://www.mcleodusa.com/html/ir/singleStory.php3?pid=147&type=press>.

⁷ McLeodUSA Press Room, “McLeodUSA Reaches Recapitalization Agreements with Forstmann Little and Secured Lenders.”
<http://www.mcleodusa.com/html/ir/singleStory.php3?pid=151&type=press>.

⁸ “McLeodUSA Shares Fall, Moody’s Downgrades Debt.”
http://dailynews.yahoo.com/h/nm/20011204/tc/telecoms_mcleodusa_dc_1.html.

⁹ XO Communications Lays Off 600; CLEC-Planet, Wayne Kawamoto (October 3, 2001).

announced a proposed restructuring plan under which Forstmann Little & Co.'s initial investment of \$1.5 billion in preferred stock would be wiped out and it and Teléfonos de México S.A. de C.V. (TELMEX) would each invest \$400 million in exchange for a 39 percent share in the company. The restructuring comes with a high price to other shareholders and bond holders. According to a recent article in The Wall Street Journal, the investment "is part of a proposed restructuring plan, which in its current state would wipe out founder Craig McCaw's investment, leave other shareholders virtually penniless and require bondholders to take a big hit."¹⁰

Investors have unambiguously indicated that they will remain wary of CLEC stocks until it becomes clearer "which CLECs will survive the carnage."¹¹ Industry experts agree that when the smoke clears from "the steady stream of Chapter 11 filings in the competitive telecom sector" only a few CLEC companies will remain.¹²

III. OUT OF REGION RBOCs HAVE FAILED TO COMPETE AGAINST FELLOW RBOCs. (PUBLIC INTEREST)

Perhaps the best indicator of the state of local competition is the extent to which ILECs choose to compete with each other. ILECs not only know the local market, but

¹⁰ Kara Scannell, "Forstmann Bets Even More of Its Money on XO," The Wall Street Journal, November 30, 2001, p. C1. Similarly, Simon Romero of The New York Times wrote that Forstmann's proposals for McLeodUSA and XO, "which largely plunder shareholders and bondholders, have sent a chill through a part of the telecommunications industry already in tatters." "A Buyout Company May Plan Some Tough Love for Two Telecoms, and Holders of Their Debt and Stock," December 10, 2001, p. C3.

¹¹ Telecom Services – Local: Hoexter's Broadband Bits, Merrill Lynch Capital markets, K. Hoexter, at *1 (June 18, 2001).

¹² Telecom Services – Alternative Carriers: Competition Telecom, Morgan Stanley, Dean Witter, P. Kennedy, at *1 (June 19, 2001).

they come equipped with the complex back-office systems needed to provide service efficiently and economically. It is telling, then, that despite earlier assertions to the contrary, the RBOCs have remained largely outside the local competition fray. Verizon does not identify any fellow RBOC as a competitor to it in Rhode Island. Qwest, SBC and Bell South have failed to establish themselves as significant providers of local service outside their serving territories. If local competition were truly enabled, these RBOCs could have entered Rhode Island and other Verizon markets with bundles of local and long distance service. Perhaps Sprint's experiences can shed some insight into why they have not done so.

Despite its extensive experience in the local markets as an incumbent LEC, Sprint has no significant CLEC operations today. On the contrary, Sprint has cut back significantly on its previously planned CLEC activities. One year ago, Sprint abandoned its local market entry via resale or UNE-P altogether. After efforts in selected states (including Georgia, New York, Texas and California), Sprint determined that entry through either of these means could not be profitable, even taking into account its ability to retain long distance customer accounts. In October of this year, Sprint announced the discontinuance of its Sprint ION residential and business offerings. Sprint had viewed Sprint ION as a breakthrough, integrated offering that promised to give consumers a superior alternative to the local offerings of ILECs. However, after extensive testing, including commercial offering of the service in a number of states, Sprint determined that it could not economically justify continuation or expansion of the service.

Among the factors contributing to Sprint's decision was the difficulty of obtaining the "last mile" facilities needed for the service from the RBOCs. No Bell Company has found it to be in its own interest to cooperate in establishing local competition. Thus, at every turn, there are lengthy delays, inadequate provision of service, and high prices. Due to the regulatory and legislative uncertainties regarding the future availability of facilities, carriers have no assurance about the level of future rates or the availability of services and service elements. Making business decisions, which require massive amounts of capital, in the face of such uncertainties is obviously very risky.

IV. COMPETITION IN RHODE ISLAND HAS NOT BEEN FIRMLY ESTABLISHED. (PUBLIC INTEREST)

As noted above, the Act allows competitors to enter the local market via three entry strategies: resale of the incumbent's network, the use of unbundled network elements, or interconnection to the incumbent's network by pure facilities-based providers, or some combination thereof. The Commission has found that all three means of entry should be available:

Congress did not explicitly or implicitly express a preference for one particular strategy, but rather sought to ensure that all procompetitive entry strategies are available. Our public interest analysis of a section 271 application, consequently, must include an assessment of whether all procompetitive entry strategies are available to new entrants.

Michigan 271 Order ¶387. In discussing how it would evaluate whether all strategies are available, the Commission made clear that there should be competition in each means of providing competitive local service and to both business and residential customers:

The most probative evidence that all entry strategies are available would be that new entrants are actually offering competitive local telecommunications services to different classes of customers (residential and business) through a variety of

arrangements (that is, through resale, unbundled elements, interconnection with the incumbent's network, or some combination thereof), in different geographic regions (urban, suburban, and rural) in the relevant state, and at different scales of operation (small and large).

Id. ¶391.

In its application, Verizon identifies eight CLEC competitors using the three strategies as evidence that the Rhode Island market is irreversibly open to competition. There are several flaws, however, in Verizon's argument that meaningful competition exists.

First, the only viable competitor for residential service is Cox Communications, the major cable provider in Rhode Island. Other CLECs identified by Verizon cater primarily to the business market. Assuming that most of the residential lines served by other carriers are either UNE Platform Lines or Resold lines, there are only approximately 6,000 lines, or approximately 1 percent of Verizon's switched lines in Rhode Island,¹³ served by CLECs other than Cox. Thus, there is virtually no competition for residential service using these two entry strategies. If the local market in Rhode Island were truly open, more meaningful entry likely would have occurred.

Second, while Cox provides its residential service to customers who do not subscribe to its cable or data services, its price for such service is higher than Verizon's. Cox's price for telephone service alone is \$19.95 per month (plus taxes and surcharges),¹⁴

¹³ Verizon state that it has approximately 630,000 switched lines in Rhode Island. Application, Appendix A, Tab F, "Local Competition in Rhode Island," ¶3.

¹⁴ Information based on a call to Cox Communications Customer Service at 401-383-2000 on December 6, 2001.

while Verizon's rates for unlimited residential service for one party range from \$12.30 to \$17.26.¹⁵ In order to obtain competitive pricing, the Cox residential customer must purchase either cable or Cox@Home service in addition to local telephone service. The rate for telephone service then decreases to "as low as \$11.95" per month for the first line and "as low as \$9.95" for the second line.¹⁶ As the basic cable package costs \$14.34 per month (Cox Limited Basic Service for \$10.75 plus converter and remote) and as Cox@Home costs \$34.95 per month (Cox customer with purchase of modem),¹⁷ customers who do not want another Cox service will not find Cox's telephone service an attractive alternative to Verizon. This is not meaningful local competition.

Nevertheless, Cox appears to provide a widespread, facilities-based competitive alternative in Rhode Island. Indeed, there are approximately 45,000 competitive residential lines alleged by Verizon, less than 6,000 of which are provided using the UNE or resale strategy. But, as discussed above, Cox's current offerings are not competitive for standalone telephone service. Given the precarious health of the segments of the CLEC industry that rely on other entry strategies -- carriers that own their own switches but use UNE loops, or use UNE-P or resale -- the business horizon is fraught with uncertainty. In particular, the pricing standards for UNEs are still in litigation, and the FCC has just commenced a review of UNE rules which raises questions about the future

¹⁵ Verizon New England Inc., Rates and Charges Effective in the State of Rhode Island, PUC RI No. 15, Part M, Section 1, pages 14-15.

¹⁶ <http://www.cox.com/NewEngland/Telephone/Pricing%20in%20Rhode%20Island.asp>.

¹⁷ <http://www.cox.com/NewEngland/NavIncludes/Providence.pdf>.

availability of various UNEs. Under these circumstances, there is a very real possibility that the market for residential service in Rhode Island could turn out to be a cable-RBOC duopoly. In the early cellular market, the duopoly did not produce competitive results. Since new wireless providers have entered the market, output has skyrocketed and a wide variety of products and pricing strategies are available to customers.¹⁸ Sprint therefore question if the public interest would truly be satisfied if only two carriers served the residential market in Rhode Island.

Finally, assuming that Cox serves primarily the residential market, most or all of the CLEC 75,000 business lines claimed by Verizon are divided among the 7 other CLECs that Verizon identifies. These lines amount to approximately 12 percent of Verizon's 630,000 switched lines (business and residential) in Rhode Island, with no CLEC having a market share greater than 2 percent. In the Michigan Order (at ¶ 77, footnote omitted), the Commission stated that "we recognize that there may be situations where a new entrant may have a commercial presence that is so small that the new entrant cannot be said to be an actual commercial alternative to the BOC, and therefore not a 'competing provider.'" Sprint does not believe it can be assumed that competitors with such very small market shares can be relied on to provide a viable alternative in the long

¹⁸ In 1998, the Commission stated that "[u]ntil a few years ago, licensed cellular providers enjoyed duopoly market power, substantially free of direct competition from any other source.*** Most recently, we have adopted a *Third CMRS Competition Report* in which we observed that the CMRS marketplace has continued to progress toward competition during the past year, with the result that prices for mobile telephony service have been falling and service offerings have become more diverse." In the Matter of Biennial Regulatory Review – Elimination or Streamlining of Unnecessary and Obsolete CMRS Regulations, et. al., 13 FCC Rcd 16857 ¶21 (footnote omitted).

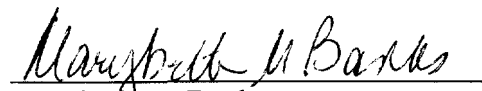
run to Verizon's local service. In addition, to the extent the CLEC lines estimated by Verizon include lines to Internet Service Providers, such lines are not an alternative for local voice service. In short, it appears that the present competitive landscape in Rhode Island may consist of a duopoly in the residential market and perhaps unviably small competitors in the business market.

V. CONCLUSION.

Because Verizon has failed to demonstrate that there is meaningful competition in Rhode Island, its application for Section 271 relief should be denied.

Respectfully submitted,

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December 17, 2001

CERTIFICATE OF SERVICE

I, Sharon Kirby, do hereby certify that this 17th day of December 2001 copies of the Comments of Sprint Communications Company L.P. on the application by Verizon for Section 271 Authorization to Provide In-Region, InterLATA Service in the State of Rhode Island and Providence Plantations, CC Docket No. 01-324, will be delivered as indicated below to the following parties:

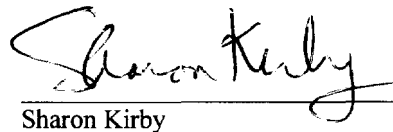
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